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Supreme Court of the United States

October Term, 1976

No. 76-763

CAMELIA BUILDERS, INC., E. J. YELVERTON, JR., FARNALE, INC., R. L. GOODALE and JEFFREY H. HUBBARD,

Petitioners,

against

FIDELITY MORTGAGE INVESTORS,

Respondent.

BRIEF FOR FIDELITY MORTGAGE INVESTORS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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No. 76-763

CAMELIA BUILDERS, INC., E. J. YELVERTON, JR., FARNALE, INC., R. L. GOODALE and JEFFREY H. HUBBARD,

Petitioners,

against

FIDELITY MORTGAGE INVESTORS,

Respondent.

BRIEF FOR FIDELITY MORTGAGE INVESTORS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Opinions Below

Camelia Builders, Inc., E. J. Yelverton, Jr., Farnale, Inc., R. L. Goodale and Jeffrey H. Hubbard, the petitioners herein (hereinafter collectively "Petitioners"), seek the issuance of a writ of certiorari to the United States Court of Appeals for the Second Circuit (the "Second Circuit") from that court's judgment and opinion issued on Septem-

ber 3, 1976. Appendix* I at 1a-22a.** The judgment of the Second Circuit affirmed an order of the United States District Court for the Southern District of New York entered on January 15, 1976. Appendix III at 32a-35a. The district court order was entered pursuant to a memorandum opinion of the district judge, dated December 16, 1975 (Appendix III at 35a-39a), and was based on evidence submitted to the district court and a "Certificate of Facts Showing Contempt" (the "Certificate") entered by the bankruptcy judge on July 29, 1975. Appendix IV at 41a-46a. The bankruptcy judge's Certificate and his "Decision of Proceeding to Certify for Contempt," dated July 14, 1975 (Appendix IV at 46a-57a), were rendered after a two-day trial held before him on April 10-11, 1975.

Jurisdiction

Although Petitioners state that jurisdiction is invoked under 28 U.S.C. §1254(1), presumably they also invoke jurisdiction under Section 24c of the Bankruptcy Act (hereinafter the "Act"), 11 U.S.C. §47(c).

Questions Presented

1. Whether the court of appeals correctly held that a knowing and wilful violation of Rule 11-44 of the Rules of Bankruptcy Procedure, 415 U.S. 1033 (1974), constitutes civil contempt.

* All references to "Appendix" refer to the appendices annexed to the petition for writ of certiorari (the "Petition") submitted by Petitioners.

** The opinion of the Second Circuit reprinted in Appendix I does not contain the correction made in the court's *per curiam* decision of November 5, 1976, which denied Petitioners' petition for rehearing. That decision, correcting page 8a of Appendix I to the Petition, is reproduced in the Appendix hereto.

2. Whether the court of appeals correctly held that Petitioners' reliance on 28 U.S.C. §959 in commencing and continuing a plenary action against Fidelity Mortgage Investors ("FMI"), debtor-in-possession, was improper.

Statutes and Rules Involved

The statutes involved are 28 U.S.C. §959 and Sections 41a(1), 70a(5), and 311 of the Bankruptcy Act, 11 U.S.C. §69a(1), 110a(5), and 711, respectively. The Rules of Bankruptcy Procedure involved are Rules 920, 810, 752(a) and 11-44. The pertinent parts of these statutes and rules are reproduced in the appropriate portions of this brief, and, except for Section 70a(5) of the Act and Rule 752(a), are also reproduced in Appendices V, VII and VIII to the Petition.

Statement of the Case

Fidelity Mortgage Investors, as debtor-in-possession under Chapter XI of the Act, respondent herein, applied to the bankruptcy court on March 28, 1975, for an order (1) adjudging Camelia Builders, Inc. ("Camelia"), E. J. Yelverton, Jr., Farnale, Inc. ("Farnale"), R. L. Goodale and Jeffrey H. Hubbard in civil contempt or, in the alternative, certifying the facts of Petitioners' contumacious conduct to the district court; (2) temporarily restraining Petitioners from proceeding with an action against FMI in the United States District Court for the Southern District of Mississippi (the "Mississippi Action"); (3) requiring Petitioners, jointly and severally, to reimburse FMI for its actual costs, expenses, disbursements and attorneys' fees

necessarily incurred in defending the Mississippi Action and in obtaining the relief it sought in the bankruptcy court; and (4) granting FMI such other and further relief as was just.

A hearing on FMI's application was held in the bankruptcy court on April 10 and 11, 1975. On July 14, 1975, based upon the testimony adduced and the other evidence admitted, the bankruptcy judge held that Petitioners' commencement of the Mississippi Action to enforce their purported lien against property* of FMI constituted contempt. Appendix IV at 56a. Because he found Petitioners' contempt to be "grave," the bankruptcy judge also held that the authorized relief under Rule 920(a)(3) of the Rules of Bankruptcy Procedure was insufficient. Appendix IV at 49a. Accordingly, on July 29, 1975, pursuant to Section 41 of the Act, 11 U.S.C. §69, and Bankruptcy Rule 920(a)(4), the bankruptcy judge certified to the district court the facts adduced at the hearing before him on April 10-11, 1975, and, on the basis of the certified facts (the "Certificate"), directed Petitioners to show cause in the district court why they should not be adjudged guilty of civil contempt. Appendix IV at 39a-41a.

On August 19, 1975, the parties presented their arguments in the district court, based on the evidence adduced in the bankruptcy court. Neither Petitioners nor FMI offered any additional testimonial evidence, although Petitioners did offer additional documentary evidence.

* FMI was a construction lender which had made a construction loan to the developer of a condominium project in Jackson, Mississippi, and held as security for the loan a first deed of trust on the Mississippi project and the land on which it was to be built. Appendix IV at 43a. Camelia and Farnale have asserted mechanics' and materialmen's liens against the subject property. *Id.*

On December 16, 1975, the district court rendered an opinion adjudging Petitioners "guilty of contempt of court" and requiring them to pay to FMI the costs, including attorneys' fees, which it incurred in the Mississippi Action and in the prosecution of the contempt proceeding. The court further required Petitioners to effect the return of certain monies which FMI had deposited with the court clerk in the Mississippi Action. Appendix at 39a. An order incorporating the relief granted by the district court was entered on January 15, 1976. Appendix III at 32a-34a.

On January 27, 1976, Petitioners filed their notice of appeal with the district court. The appeal was argued before the Second Circuit on May 13, 1976. A decision was rendered on September 3, 1976, affirming the decision of the district court in all respects. Thereafter, Petitioners petitioned the Second Circuit for rehearing and rehearing *en banc*. The court denied both petitions on November 5, 1976. Appendix II at 30a-31a.

On December 6, 1976, Petitioners filed the Petition with the clerk of the Supreme Court of the United States.

Petitioners' commencement and continuation of the Mississippi Action in contravention of Rule 11-44 constituted the conduct which was the basis of the contempt proceeding. Petitioners commenced the Mississippi Action on March 25, 1975, almost two months after FMI filed its Chapter XI petition.* They had actual knowledge, at the time, of the pending Chapter XI case and the automatic stay provisions of Rule 11-44. Appendix IV at 44a-45a. Despite such knowledge, Petitioners wilfully and deliberately violated

* FMI filed its Chapter XI petition on January 30, 1975.

the stay provisions by proceeding with the Mississippi Action, thereby depriving FMI and its creditors of $75,964.33 which FMI was required to deposit with the Mississippi federal court and also causing FMI to incur unnecessary legal fees and related expenses.

All other material facts in the instant case are set forth in the Certificate (Appendix IV at 41a-46a) and in the opinion of the Second Circuit (Appendix I at 1a-29a).

Summary of Argument

I.A. The court of appeals properly affirmed the district court's civil contempt judgment against Petitioners. Upon the filing of FMI's Chapter XI petition, Rule 11-44 automatically stayed "the commencement or the continuation of any court or other proceeding against [FMI] . . . or to enforce any lien against [FMI's] property"—wherever located. *See* Section 311 of the Act, 11 U.S.C. §711. Petitioners' commencement of the Mississippi Action against FMI, with the avowed purpose of affecting FMI's property, a first deed of trust (mortgage) on real property, with actual knowledge of the pendency of the FMI Chapter XI case as well as the provisions of Rule 11-44, constituted civil contempt under Section 41a(1) of the Act, 11 U.S.C. §69 (a)(1), subjecting Petitioners to the sanctions of Rule 920.

FMI's first deed of trust was "property" within the meaning of the Act. "[T]he term 'property' has been construed most generously and an interest is not outside its reach because it is novel or contingent or because enjoyment must be postponed." *Segal* v. *Rochelle*, 382 U.S. 375, 379

(1966). "Certainly, [a mortgage] interest constitutes 'property' . . . as 'property' can constitute something other than fee ownership." *In re Westec Corp.*, 460 F.2d 1139, 1143 (5th Cir. 1972).

The automatic stay of suits contained in Rule 11-44 is clear and specific. Virtually identical automatic stays contained in Bankruptcy Rules 401 and 601 have been enforced by means of contempt proceedings. *In re Tallyn*, 2 Bankr. L.Rep. ¶65,617 (E.D.Va. 1975); *In re Young*, 1 Collier Bankruptcy Cases 145 (M.D. Fla. 1974).

Rule 11-44(e) provides for immediate *ex parte* relief from the automatic stay, upon an appropriate factual showing, in order to avoid hardship to any person. Petitioners admittedly sought no such relief.

The court of appeals properly affirmed the district court's application of Bankruptcy Rule 920 in holding Petitioners liable for civil contempt. Such a "purely remedial" judgment is "analogous to a tort judgment for damages caused by wrongful conduct." *Parker* v. *United States*, 153 F.2d 66, 70 (1st Cir. 1946).

I.B. The Mississippi Action did not arise out of an act of FMI, as debtor-in-possession, in carrying on its business, and, therefore, 28 U.S.C. §959 did not authorize Petitioners' suit against FMI. FMI was merely performing its statutory duty as debtor-in-possession when it foreclosed its deed of trust. 8 Collier, Bankruptcy ¶6.32 at 928-929 (14th rev. ed. 1975). To preserve or "to collect and liquidate the assets of a debtor is not to carry on its business in any proper sense of the term." *Austrian* v. *Williams*, 216 F.2d 278, 285 (2d Cir. 1954), *cert. denied*, 348 U.S. 953 (1955).

II. The decision of the Second Circuit here is in accord with the decisions of this Court and of the other circuits. *Mueller* v. *Nugent*, 184 U.S. 1, 14 (1902) ("the filing of the petition is a *caveat* to all the world, and in effect an attachment and injunction. . . ."); *In re Rubin*, 378 F.2d 104, 108 (3d Cir. 1967).

Argument

I.

The Decision Below Is Correct.

A. A Knowing and Wilful Violation of Chapter XI Rule 11-44 Constitutes Contempt.

1. The Automatic Stay of Suits in Rule 11-44 Is Clear and Specific.

Upon FMI's filing its Chapter XI petition under Rule 11-6, the automatic stay of actions against the debtor and stay of lien enforcement against the debtor's property contained in Rule 11-44 immediately became effective. Rule 11-44 provides, in pertinent part, as follows:

> *Rule 11-44. Petition as Automatic Stay of Actions Against Debtor and Lien Enforcement.*
>
> *(a) Stay of Actions and Lien Enforcement.* A petition filed under Rule 11-6 or 11-7 shall operate as a stay of the commencement or the continuation of any court or other proceeding against the debtor, or the enforcement of any judgment against him, or of any act or the commencement or continuation of any court proceeding to enforce any lien against his property, or of any

> court proceeding, except a case pending under Chapter X of the Act, for the purpose of the rehabilitation of the debtor or the liquidation of his estate.

The language of Rule 11-44(a) is clear and unequivocal. Thus, Petitioners' commencement of the Mississippi Action against FMI with full knowledge of the pendency of the FMI Chapter XI case was a direct violation of the provisions of Rule 11-44 and constituted contempt,* punishable under Bankruptcy Rule 920, made applicable to Chapter XI cases by Rule 11-63. Rule 920(a) provides, in pertinent part, as follows:

> *(2) Disposition by Referee upon Notice and Hearing.* Any other conduct prohibited by §41a of the Act** may be punished by the referee only after hearing on notice. The notice shall be in writing and shall state the time and place of hearing, allowing a reasonable time for the preparation of the defense, and shall state the essential facts constituting the contempt charged and whether the contempt is criminal or civil or both. The notice may be given on the referee's own initiative or on motion by a party, by the United States attorney, or by an attorney appointed by the referee for that purpose. If the contempt charged involves disrespect to or criticism of the referee, he is disqualified from presiding at the hearing except with the consent of the person charged.

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* On March 18, 1974, this Court entered an order promulgating the Rules of Bankruptcy Procedure for Chapter XI cases and making them effective in all such cases "on July 1, 1974." 415 U.S. 1005 (1974). The bankruptcy court also entered an order on February 28, 1975, which, among other things, fixed a date for the first meeting of creditors in the FMI Chapter XI case, and noted that the Rule 11-44 automatic stay of suits was effective on January 30, 1975, the date on which FMI filed its Chapter XI petition.

** Section 41a(1) of the Act, 11 U.S.C. §69(a)(1), provides in relevant part that "[a] person shall not . . . disobey or resist any lawful order, process or writ."

(3) Limits on Punishment by Referee. A referee shall not order imprisonment nor impose a fine of more than $250 as punishment for any contempt, civil or criminal.

(4) Certification to District Judge. If it appears that conduct prohibited by §41a of the Act may warrant punishment by imprisonment or by a fine of more than $250, he may certify the facts to the district judge. On such certification the judge shall proceed as for a contempt not committed in his presence.

The courts have consistently enforced the contempt provisions of Section 41a(1). *See Mueller* v. *Nugent,* 184 U.S. 1 (1902); *In re Rubin,* 378 F.2d 104 (3d Cir. 1967); *Docteroff* v. *New York Credit Men's Adjustment Bureau,* 187 F.2d 4 (2d Cir. 1951); *In re American Associated Systems, Inc.,* 373 F.Supp. 977 (E.D. Ky. 1974); *In re Lawrence Carpet Co.,* 122 F.Supp. 912 (S.D.N.Y. 1954); *In re Sussman,* 85 F.Supp. 570 (S.D.N.Y. 1949); 1 Collier, Bankruptcy ¶¶2.57, 2.58 at 302.4-321 (14th rev. ed. 1974); 2A Collier, Bankruptcy ¶¶41.01, 41.03 at 1583, 1589 (14th rev. ed. 1974); *see also United States* v. *Ross,* 243 F.Supp. 496, 499 (S.D.N.Y. 1965) ("A 'civil contempt' is a litigant's failure to do something ordered to be done in a civil action for the benefit of the opposing party therein.").

The decision of the court of appeals here, which affirmed the district court's civil contempt judgment, is correct. The Second Circuit recognized the settled rule that in order to cite a party for contempt it must be established that (a) the alleged contemnor had knowledge of the order which he is said to have violated, (b) the order was specific and definite, and (c) the alleged contemnor violated the order.

In re Rubin, 378 F.2d 104, 108 (3d Cir. 1967) (cited with approval in the Petition at 17 and 21).

The court of appeals correctly found here that all three requirements were satisfied: (a) The evidence at the trial "amply documented knowledge on the part of [Petitioners] of FMI's Chapter XI petition and the consequent stay under Rule 11-44." Appendix I at 7a; (b) "It is difficult to conceive of a rule with a more apparent and certain meaning: After the Chapter XI petition has been filed, a debtor cannot be sued." Appendix I at 6a; and (c) "Rule 11-44 clearly required Camelia and Farnale to secure the permission of the New York bankruptcy court before filing an action against FMI in Mississippi." Appendix I at 21a-22a.

2. *The Bankruptcy Court Had Jurisdiction to Hold Petitioners in Civil Contempt*

Petitioners urge that the bankruptcy court lacked authority and jurisdiction to enter a civil contempt judgment for a violation of Rule 11-44. Petition at 7-12. They cite no applicable authority for this contention, however, for none exists.

In fact, courts have uniformly held that a violation of the injunctive provisions of the Rules of Bankruptcy Procedure, specifically Rules 401 and 601, does constitute contempt, subjecting the contemnor to the sanctions of Bankruptcy Rule 920. *See In re Tallyn,* 2 Bankr. L. Rep. ¶65,617 (E.D. Va. 1975); *In re Young,* 1 Collier Bankruptcy Cases

145 (M.D. Fla. 1974). Bankruptcy Rules 401 and 601* are, by their terms, the virtual equivalent of Rule 11-44. Thus, Petitioners' violation of the injunctive provisions of Rule 11-44** should, as the court of appeals correctly reasoned, subject them to the sanctions of a civil contempt judgment.

> Since Rule 11-44 has the effect of an order and was designed to expedite automatically the stay that would otherwise be obtained by an order,[2] it would be exalting form over substance to hold that a violation of Rule 11-44 is not punishable under §41(a) and Rule 920. . . .
>
> In short, . . . the contempt power of the courts under §41(a) and Rule 920 includes the authority to enforce the rules themselves via contempt orders.

2 For a discussion of court orders designed to stay subsequent proceedings against debtors-in-possession, see 1 Collier, *Bankruptcy,* 2.62 (14th ed. 1972). For the purposes of our opinion, the important point is that Rule 11-44 now makes the establishment of such stays automatic. In the absence of such automatic stays, the debtors-in-possession secured specific orders to the same effect. We see no reason to treat a stay explicitly granted by the court differently from a stay established by rule, at least with respect to the courts' enforcement powers via contempt.

Appendix I at 10a.

* Bankruptcy Rules 401 and 601 read in pertinent part as follows:

> *Rule 401.* . . . The filing of a petition shall operate as a stay of the commencement or continuation of any action against the bankrupt. . . .
>
> *Rule 601.* . . . The filing of a petition shall operate as a stay of any act or the commencement or continuation of any court proceeding to enforce . . . a lien against property in the custody of the bankruptcy court. . . .

** Rule 11-44 was promulgated pursuant to Section 2075, Title 28, United States Code, by *order* of the Supreme Court of the United States on March 18, 1974, and became effective on July 1, 1974. 415 U.S. 1033 (1974).

Petitioners rely on two inapposite cases in an attempt to limit the contempt powers of the bankruptcy and district courts. Both cases, *Wakefield* v. *Housel,* 288 F. 712 (8th Cir. 1923), and *Magen* v. *Campbell,* 186 F. 675 (3d Cir. 1911) (Petition at 9-10), involved *criminal* contempt convictions in contrast to the *civil* contempt judgment here. The courts in *Magen* and *Wakefield* objected to the denial to the alleged contemnors of the additional rights available to criminal defendants. Aside from being distinguishable on their facts, the legal reasoning in *Magen* and *Wakefield* is inapplicable here. Neither case involved a violation of the Rules of Bankruptcy Procedure and the automatic stay of lien enforcement provided for therein. Because the charge was criminal contempt in *Wakefield,* for which a person may be sentenced, as a punitive measure, to a definite term of imprisonment, the court held that the alleged contemnor was entitled to be charged with a "criminal act or acts with such clearness and certainty as to advise the accused of the charge which he had to meet and to give him a fair opportunity to prepare his defense." 288 F. at 717. In contrast, Petitioners have not claimed—and, indeed, cannot claim—that they were deprived of a fair opportunity to defend themselves.

Petitioners also argue that the bankruptcy court lacked jurisdiction because FMI's property, upon which Camelia and Farnale were attempting to enforce their asserted liens, was purportedly "in custodia legis of the State Court prior to the institution of the Chapter XI proceeding." Petition at 10-11. Petitioners, however, ignore Section 311 of the Bankruptcy Act, 11 U.S.C. §711, which gives the Chapter XI court "exclusive jurisdiction of the debtor and [its]

property, *wherever located.*" (Emphasis supplied.) As the Second Circuit stated here, "§311 deprived the Mississippi state court of the jurisdiction which it [had] exercised until [FMI filed its Chapter XI petition]." Appendix I at 11a. Thus, because Rule 11-44, which is based on the broad jurisdictional grant of Section 311, enjoins "the commencement or the *continuation* of any court or other proceeding against the debtor . . ." (emphasis supplied), FMI's filing of a Chapter XI petition stayed not only the commencement of the Mississippi Action, but also Petitioners' *continuing* their suit in the Mississippi state court,* commenced prior to the FMI Chapter XI case.

Although Petitioners contend that the "Second Circuit appears to have misconstrued the entire nature of the proceeding before them" (Petition at 11), it is Petitioners who misunderstand the applicable law. Petitioners mistakenly cite *Straton* v. *New*, 283 U.S. 318 (1931), which was decided before the passage of the Chandler Act in 1938, and which dealt with the bankruptcy court's powers in an ordinary bankruptcy case under Chapters I-VII of the Act. As the Court stated in *Straton*:

> The filing of the petition is an assertion of jurisdiction. . . . *This jurisdiction is exclusive within the field defined by the law, and is so far in rem that the estate is regarded as in custodia legis from the filing of the petition.* [Citation omitted.] It follows that liens cannot thereafter be obtained nor proceedings be had in other courts to reach the property, the

* In January of 1975, shortly before FMI filed its Chapter XI petition, Camelia and Farnale, as a joint venture, sued FMI in the Circuit Court of Rankin County, Mississippi, seeking (1) an order enforcing their purported lien, and (2) a monetary judgment against FMI. Appendix IV at 43a.

> district court having acquired the exclusive right to administer all property in the bankrupt's possession. [Citation omitted, emphasis supplied.]

283 U.S. at 321. The jurisdiction of the bankruptcy court in *Straton* was thus restricted to administering "all property *in the bankrupt's possession.*" 283 U.S. at 321 (emphasis supplied). In contrast, the Chapter XI court here, vested with the broader jurisdiction given it by Section 311, could stay Petitioners from proceeding against FMI and its property in Mississippi. *See generally* 8 Collier, Bankruptcy ¶3.01[1] at 146-7 (14th rev. ed. 1974).

Petitioners also misconstrue several other cases in their attempt to show that the Chapter XI court here had no jurisdiction to stay them from commencing the Mississippi Action. They misread *In re A. Roth Co.*, 125 F.2d 396 (7th Cir. 1942) (Petition at 12), which was not a contempt proceeding, but rather a lienholder's application to the bankruptcy court for leave to foreclose on a mortgage. The court in *Roth* specifically noted as follows:

> It has long been the practice that when one desires to make the trustee a party to a foreclosure suit, to first obtain permission from the Bankruptcy Court.

125 F.2d at 397. Thus, had the lienholder in *Roth* proceeded with a foreclosure action without seeking leave of the bankruptcy court, he would have been in contempt. The lienholder in *Roth*, however, unlike Petitioners, *did* seek relief from the bankruptcy court's stay of lien enforcement before proceeding in another court. 125 F.2d at 397-98. Although the court of appeals in *Roth* found the bankruptcy court's denial of leave to foreclose to be an abuse of discretion, the court never denied the necessity of applying to the

bankruptcy court for leave to foreclose. In fact, the court confirmed its belief in that requirement. *Id,* at 397.

Petitioners have similarly misread *Town of Agawam* v. *Connors,* 159 F.2d 360 (1st Cir.), *cert. denied,* 330 U.S. 845 (1947) (Petition at 12), which also did not involve a contempt proceeding. In *Agawam,* another ordinary bankruptcy case under Chapters I-VII of the Act, the court held that the bankruptcy court could not interfere with a state court action when *in rem* jurisdiction had attached more than four months prior to the filing of the bankruptcy petition. 159 F.2d at 363-64. Sueh facts do not appear here, for the Mississippi Action was commenced by Petitioners *after* the filing of FMI's Chapter XI petition.

Because *Agawam* was a bankruptcy case, and *not* a Chapter XI case, the bankruptcy court's jurisdiction there was based on property in the actual or constructive possession of the debtor at the date of bankruptcy. *See Ex parte Baldwin,* 291 U.S. 610, 615 (1934); Mussman & Riesenfeld, Jurisdiction in Bankruptcy, 13 Law & Contemp. Prob. 88, 92, 98 (1948); MacLachlan, Bankruptcy 205 (1956). In the Chapter XI case here, the bankruptcy court had the much broader jurisdiction over FMI's property "wherever located," pursuant to Section 311 of the Act. *In re Stockman Development Co.,* 447 F.2d 387, 390 (9th Cir. 1971); *Slenderella Systems of Berkeley, Inc.* v. *Pacific T&T Co.,* 286 F.2d 488, 489-90 (2d Cir. 1961). Furthermore, the bankrupt in *Agawam* did not have the broad protection of Rule 11-44. The stay given the bankrupt in *Agawam,* based on Section 11a of the Act, only protected it against certain actions on *unsecured* debts, whereas Rule 11-44 provides FMI with an

automatic stay of *all* suits against the debtor and its property, even if such property is not in its possession.

> Any act to enforce the lien, such as commencement of foreclosure, seizure of the property subject to the lien, or an attempt to sell the property even though seized prior to the filing of the petition would be violation of the automatic stay. It matters not that foreclosure proceedings were instituted prior to the filing of the Chapter XI petition, for Rule 11-44 includes "continuation of any court proceeding to enforce any lien against the debtor's property" within the broad scope of the stay.

8 Collier, Bankruptcy ¶3.22, at 261 (14th rev. ed. 1974).

Petitioners' reliance on *Mid-Jersey National Bank* v. *Fidelity Mortgage Investors,* 518 F.2d 640 (3d Cir. 1975), is also misplaced. *Mid-Jersey* involved FMI's deposit of money with the court *after* entry of judgment against FMI and *before* FMI filed its Chapter XI petition. As the Second Circuit noted, in *Mid-Jersey,* the deposit was "the *res* of a trust held by the district court. Since the deposit was not FMI's property, it was not within the jurisdiction of the bankruptcy court under §311 and, therefore, Rule 11-44 was held inapplicable to the appeal." Appendix I at 14a. Here, unlike *Mid-Jersey,* "FMI, as holder of a deed of trust, had a property interest . . . which gave the bankruptcy court jurisdiction under §311." Appendix I at 14a. In contrast to *Mid-Jersey,* no judgment had ever been rendered against FMI in either the Mississippi Action or the state court action, and no money of FMI had been deposited with the court prior to the commencement of the FMI Chapter XI case. Rather, FMI was forced to deposit the sum of $75,964.33 with the Mississippi federal court as a direct

result of Petitioners' conduct, *after* the FMI Chapter XI case was commenced.

In another attack on the jurisdiction of the bankruptcy court, Petitioners assert that FMI did not have a property interest involved in the Mississippi Action. Relying primarily on this Court's holding in *Segal* v. *Rochelle,* 382 U.S. 375 (1966), the court of appeals properly rejected Petitioners' argument and held that FMI's mortgage interest did "constitute 'property' within the meaning of the bankruptcy laws." Appendix I at 12a.

Petitioners rely upon *Brunn* v. *Wichser,* 75 F.2d 25 (3d Cir. 1934), to assert that FMI's first mortgage (characterized as a first deed of trust) on real property, which secured a loan in the principal amount of $1,600,000, is not "property" of the debtor,* and that, therefore, the bankruptcy court had no jurisdictional basis** on which to stay them from prosecuting the Mississippi Action. The applicable authorities, however, conclusively demonstrate that a mortgage is "property," and that it is a sufficient jurisdictional basis for a Chapter XI court to stay litigation in other courts.

Brunn, supra, a pre-Chandler Act case involving an extension of time to pay debts, was, in effect, overruled by this Court in *Segal* v. *Rochelle, supra,* by the Second Circuit in *In re Prudence-Bonds Corp.,* 77 F.2d 328, 330 (2d Cir.), *cert. denied,* 296 U.S. 584 (1935) (holding that mortgages

* In fact, FMI now has title to the real property in question by virtue of a foreclosure sale held on March 28, 1975.

** Rule 11-44 is broadly worded so as to stay suits "against the debtor" *or* its "property," thereby indicating that any suit against the debtor, regardless of whether it has any property, will be stayed.

are property of the debtor and actions affecting them may be stayed), and by the Fifth Circuit in *In re Westec Corp.,* 460 F.2d 1139 (5th Cir. 1972) (discussed *infra*).

In *Segal* v. *Rochelle,* this Court held that a loss-carryback tax refund of the bankrupt was property within the meaning of Section 70a(5) of the Act, 11 U.S.C. 110a(5), so that title thereto vested in the trustee in bankruptcy. In discussing the general concept of property, Mr. Justice Harlan stated for the Court as follows:

> Admittedly, in interpreting Sec. 70a(5), "[i]t is impossible to give any categorical definition to the word 'property,' nor can we attach to it in certain relations the limitations which would be attached to it in others." [Citations omitted.] Whether an item is classified as "property" by the Fifth Amendment's Just-Compensation Clause or for purposes of a state taxing statute cannot decide hard cases under the Bankruptcy Act, whose own purposes must ultimately govern.
>
> The main thrust of §70a(5) is to secure for creditors everything of value the bankrupt may possess in alienable or leviable form when he files his petition. *To this end the term "property" has been construed most generously and an interest is not outside its reach because it is novel or contingent or because enjoyment must be postponed.* [Emphasis supplied.]

382 U.S. at 379. Thus, FMI's first deed of trust (or mortgage), which represented at least a contingent interest in realty, must fall within the definition of property under the Act. In this case, FMI's mortgage portfolio is its most significant asset, and the one asset in which FMI's creditors have the greatest interest. To deprive FMI's creditors of the bankruptcy court's protection for such assets would be to subvert a major purpose of the Act: "to secure for

creditors everything of value the [debtor] may possess in alienable or leviable form when [it] files [its] petition." 382 U.S. at 379.

In *In re Westec Corp.*, 460 F.2d 1139 (5th Cir. 1972), a Chapter X case, the court held that the bankruptcy court had jurisdiction to set aside a local taxing authority's completed tax sale of certain property on which the debtor* held first and second mortgages. The court noted that Sections 111 and 148 of the Act, 11 U.S.C. §§511, 548, not only give the Chapter X court "exclusive control over all property of the debtor wherever located, but also establish an automatic stay without notice of any pending proceeding and the commencement of any further proceeding to enforce a lien against the debtor's property. . . ." 460 F.2d at 1142. Section 311 of the Act and Rule 11-44, applicable here, also give the Chapter XI court the identical powers conferred by Sections 111** and 148 of the Act in Chapter X cases. *See also* Bankr. R. 10-601.

The *Westec* court, relying in part upon *Segal* v. *Rochelle*, *supra*, concluded that a mortgage lien, even though subordinate to a statutory tax lien, was property subject to the jurisdiction of the bankruptcy court, reasoning as follows:

> The Trustee here, at the time of the foreclosure, held the first and second mortgage on the real estate in question. Certainly, this interest constitutes "property" within the meaning of Sections 111 and 148 of the Bankruptcy Act, as "property" can constitute something other than fee ownership. [Citations omitted.]

460 F.2d at 1143. After noting that the debtor in *Westec* had not filed a copy of the reorganization court's restraining order in the public records of the appropriate county, the court found that the taxing authority nevertheless had *knowledge* of the Chapter X case. 460 F.2d at 1141, 1143. Accordingly, the court held notice was not necessary, and found that the taxing authority was required to seek a modification of the restraining order if it wished to foreclose on its asserted lien. "[T]he technicalities of state law simply cannot take precedence over the restraining order issued by the Chapter X court." 460 F.2d at 1143.

. Petitioners here do not contest FMI's first deed of trust, nor do they deny that property of the debtor is within the "exclusive" jurisdiction of the Chapter XI court. Moreover, as the foregoing authorities conclusively demonstrate, FMI's first deed of trust was "property" within the meaning of the Act. Petitioners also do not dispute that by commencing the Mississippi Action, they were attempting to subordinate FMI's first lien to their asserted mechanics' and materialmen's lien against the subject property, which now belongs to FMI. Appendix IV at 44a, 48a. Accordingly, the bankruptcy court had jurisdiction to stay Petitioners from enforcing their asserted lien.*

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* After the debtor filed its Chapter X petition in *Westec*, a reorganization trustee took charge of its property. When FMI filed its petition, however, it continued in possession of its property as "debtor-in-possession." Sections 342, 343 of the Act, 11 U.S.C. §§742, 743.

** Like Section 311, Section 111 of the Act gives the Chapter X court "exclusive jurisdiction of the debtor and its property, wherever located."

* FMI does not concede the validity of the lien asserted by Petitioners. Even if the lien were valid, however, that fact would have no bearing on the issue of Petitioners' contempt.

3. Rule 11-44 Is Constitutional.

Mistakenly relying on *Sniadach* v. *Family Finance Corp.*, 395 U.S. 337 (1969), *Fuentes* v. *Shevin*, 407 U.S. 67 (1972), and *North Georgia Finishing, Inc.* v. *Di-Chem, Inc.*, 419 U.S. 601 (1975), Petitioners argue that Rule 11-44 is unconstitutional because it would deprive them of their right to possession of property without any remedy.

The automatic stay contained in Rule 11-44 does not deprive Petitioners of any substantive rights, nor does it leave them without remedies for any wrongs they believe FMI committed against them. Petitioners could have applied to the bankruptcy court as early as January 31, 1975, when they first became aware that FMI filed a Chapter XI petition (Appendix at 44a-45a), in order to obtain relief from the Rule 11-44 automatic stay or to pursue their claim in the bankruptcy court. Sections (d) and (e) of Rule 11-44 specifically provide for such relief. Section (d) gives priority to hearing applications for relief from the stay and further places the burden of proof on the party seeking continuation of the stay of lien enforcement. Thus, FMI would have to show, without delay, why the stay should be continued.

Section (e) of Rule 11-44 also permits *ex parte* relief from the stay if the claimant can demonstrate that "immediate and irreparable injury, loss or damage" would result before the opposing party could be heard. Petitioners chose not to pursue any of the available relief, but, on March 25, 1975, nearly two months after learning of the FMI Chapter XI case, commenced the Mississippi Action,

cavalierly disregarding the terms of Rule 11-44, of which they had actual knowledge. Appendix IV at 45a.

None of the cases cited by Petitioners is applicable here. *Sniadach, supra,* involved a challenge to a Wisconsin prejudgment wage garnishment procedure under which the defendant's salary was withheld without notice and without a prior hearing as to the probable validity of the claim. This Court characterized the garnishment as "a taking which may impose tremendous hardships on wage earners with families to support." 395 U.S. at 353. Petitioners have no such compelling argument here. On the contrary, Petitioners had *ex parte* relief which was immediately available to them in the bankruptcy court, but chose to take another course.

This Court in *Fuentes, supra,* similarly sought to protect individuals from state replevin laws which authorized summary seizure of goods on an *ex parte* application. In a four to three decision, the Court found that such a procedure violated the due process clause of the Fourteenth Amendment because the "statutes serve no . . . important governmental or general public interest." 407 U.S. at 557. Congress and this Court have determined, however, that the bankruptcy court's injunctive powers *do* serve an important general public interest. *Continental Illinois National Bank & Trust Co.* v. *Chicago, Rock Island & Pacific Ry.*, 294 U.S. 648 (1935); Murphy, Restraint and Reimbursement: The Secured Creditor in Reorganization and Arrangement Proceedings, 30 Bus. Law. 15, 19-22 (1974); Countryman, Real Estate Liens in Business Rehabilitation Cases, 50 Am. Bankr. L.J. 303 (1976). As the Court in

Fuentes noted, the "prejudgment replevin provisions work a deprivation of property without due process of law insofar as they deny the right to a prior opportunity to be heard before chattels are taken from their possessor. *Our holding, however, is a narrow one.*" 407 U.S. at 579 (emphasis supplied).

North Georgia Finishing, Inc. v. *DiChem, Inc., supra,* another non-bankruptcy case, involved an unconstitutional state prejudgment garnishment procedure, and is distinguishable on the same basis as *Sniadach* and *Fuentes, supra.* Moreover, the statute in *North Georgia Finishing* was far different from Rule 11-44 with all of its procedural safeguards, particularly section (e) which permits *ex parte* relief from the stay on a showing of "immediate and irreparable injury, loss or damage."

Petitioners thus had adequate relief available under Rule 11-44(d)-(e). As the court of appeals here correctly held:

> Rule 11-44 provides for an immediate hearing and relief from any hardship that an automatic stay might cause. In short, there is no constitutional infirmity in Rule 11-44 since that rule itself gives the creditors an immediate opportunity to have the stay lifted or modified and since the policy considerations requiring such initial stays are not insignificant.

Appendix I at 16a. Petitioners were aware of the terms of Rule 11-44, but commenced the Mississippi Action, regardless of the consequences. Their knowing refusal to take the proper steps to obtain relief is hardly a violation of their rights, as they contend.

4. Rule 920 Is Constitutional and Was Constitutionally Applied.

Petitioners set forth a baseless Fifth Amendment "double-jeopardy" argument. Petition at 33-36. Significantly, they do not cite a single case in support of their novel theory. Petitioners contend that their rights were violated because the bankruptcy court found that their contumacious conduct was so grave that it required stronger sanctions than the bankruptcy court could administer and, therefore, it certified the facts to the district court. The district court offered Petitioners the opportunity to present additional evidence. They did so, but made no request to submit additional testimonial evidence. As the court of appeals stated:

> When stripped to its essentials, Camelia and Farnale's claim is that due process is violated when a contemnor is given too many opportunities to present his side of the case. This is a rather novel theory of due process.

Appendix I at 17a. Based upon the bankruptcy court's certificate of facts and upon the additional evidence submitted by Petitioners, the district court held Petitioners in contempt, required them to cause the return to FMI of those funds deposited with the Mississippi federal court, and assessed Petitioners with FMI's costs and legal fees. Petitioners contend, however, that the provision of Rule 920 which provides for a certification of facts to the district court and the imposition of a penalty by the district court is prohibited by the double-jeopardy provision of the Fifth Amendment. If this argument were applied to criminal cases, every time a jury found a defendant guilty and a

judge imposed a sentence, the defendant would have a Fifth Amendment double-jeopardy argument.

Petitioners' argument that the district court erred in accepting the bankruptcy court's findings of fact, instead of conducting a trial *de novo* (Petition at 22-24), is similarly fallacious. Petitioners had a full, complete and fair trial in the bankruptcy court on April 10-11, 1975, in accordance with Rule 920(a)(2). Petitioners do not allege otherwise.

In his decision of July 29, 1975, the bankruptcy judge found that the punishment available to him under Rule 920(a)(3) was insufficient, in view of Petitioners' conduct. Appendix IV at 49a, 56a. Pursuant to Rule 920(a)(4), the bankruptcy judge certified his findings of fact to the district court which held that such facts constituted contempt and gave the appropriate restitution to FMI for the injuries it suffered as the result of Petitioners' conduct. As is evident from the decision of the district judge (Appendix III at 35a-39a), he analyzed the facts as set forth in the Certificate. Although the district judge found the facts not to be clearly erroneous, he drew his own conclusions from those facts and additional documentary evidence offered by Petitioners before he applied the law and determined that Petitioners were in civil contempt. Unlike the criminal contempt cases frequently cited by Petitioners, a civil contempt judgment such as the one here, is "somewhat analogous to a tort judgment for damages caused by wrongful conduct." *Parker* v. *United States,* 153 F.2d 66, 70 (1st Cir. 1946). The purpose of a contempt judgment is "purely remedial—to coerce obedience to a decree . . . or to compensate complainant for loss

caused by respondent's disobedience of such a decree." *Id.,* 153 F.2d at 70. *See also Maggio* v. *Zeitz,* 333 U.S. 56 (1948); *Oriel* v. *Russell,* 278 U.S. 358 (1929).

Bankruptcy Rule 810 provides that on appeals to the district court, "the court shall accept the referee's findings of fact unless they are clearly erroneous, and shall give due regard to the opportunity of the referee to judge the credibility of the witnesses." Logically, Rule 810 also should apply to a bankruptcy judge's certification of facts to the district court. Bankruptcy Rule 752(a), also dealing with findings of fact, has the same effect: "Findings of fact shall not be set aside unless clearly erroneous. . . ." Thus, the district court's acceptance of facts set forth in the Certificate was entirely proper.

In *In re Roark,* 28 F.Supp. 515, 518 (E.D. Ky. 1939), the court stated the general rule which is still applicable under the Rules of Bankruptcy Procedure:

> As to the ruling of the referee requiring the bankrupt and his wife to make restitution to the estate to the extent of $500, the applicable rule is that the court should not disturb the findings of the referee upon disputed issues of fact, "unless there is most cogent evidence of mistake and miscarriage of justice." Kowalsky v. American Employers Ins. Co., 6th Cir., 90 F.2d 476, 479. Realizing that the referee, having heard the witnesses in person, is in a much better position than the court to determine the credibility of witnesses and the truth as to disputed facts, I am unable to say that the action of the referee in this respect is clearly erroneous, and hence the petition for review is denied and the referee's order approved and confirmed in this respect.

Similarly, in *Mazer* v. *United States,* 298 F.2d 579, 581-82 (7th Cir. 1962), the court said:

> Initially appellant contends that the evidence does not support the findings of fact. The standard by which the referee's findings of fact are to be judged is whether they are clearly erroneous. [Citations omitted.]

See Allen v. *Lokey,* 307 F.2d 353, 354 (5th Cir. 1962) (Applying former General Order in Bankruptcy No. 47, from which Rule 810 is derived, the court held that it was unable to "set aside the referee's findings if they are not 'clearly erroneous.' ").

The Certificate of the bankruptcy judge was based upon the undisputed evidence and on Petitioners' own testimony. Thus, the court of appeals properly concluded that Rules 810 and 752(a) are applicable here, that the bankruptcy court's findings of fact were not clearly erroneous, and that Petitioners were guilty of civil contempt.

The court of appeals correctly distinguished its earlier decision* in *O'Hagen* v. *Blythe,* 354 F.2d 83 (2d Cir. 1965), on which Petitioners erroneously rely. Appendix I at 8a, and Petition at 23. *O'Hagen* involved a criminal, and *not* a civil contempt citation. It is not applicable here because it was decided prior to October 1, 1973, the effective date of the Bankruptcy Rules. Moreover, the *O'Hagen* decision was based on the premise that the bankruptcy court had *no* power to adjudge and punish anyone for contempt, a premise which has been superseded by Bankruptcy Rule 920. According to the court in *O'Hagen,*

* In fact, the Honorable J. Joseph Smith, Circuit Judge, who wrote the court's opinion, was on the panel that decided *O'Hagen.*

> There is, of course, the general principle of bankruptcy law that
>
> > "* * * the report of a referee * * * shall set forth his findings of fact and conclusions of law, and the [district] judge shall accept his findings of fact unless clearly erroneous. * *" [Citations omitted.]
>
> Punishment for contempt, following a certificate by a Referee, does not however, come within this rule. The Referee has no power to punish for contempt. [Citations omitted.]

354 F.2d at 84. Under Rule 920, however, the bankruptcy judge is now empowered to adjudge *and punish* civil contempt. Here, the bankruptcy judge merely found that Petitioners were guilty of contempt. Appendix IV at 56a. The *O'Hagen* case, therefore, is not applicable.

Moreover, the court in *O'Hagen* was not bound by the bankruptcy court's findings because the bankruptcy judge there had failed to make a factual determination as to one material element for the finding of contempt. 354 F.2d at 84-85. Petitioners make no such argument here, for they cannot.

Petitioners also cite *In re McIntosh,* 73 F.2d 908 (9th Cir. 1934) (Petition at 23), which like *O'Hagen, supra,* was a criminal contempt case decided long before Rules 920, 752(a) and 810 went into effect. Even in other criminal contempt cases, *McIntosh, supra,* has been restricted to its narrow facts. *See In re Timmerman,* 302 F.2d 663, 666 (7th Cir.) (Kiley, C.J., concurring), *cert. denied,* 371 U.S. 816 (1962). Because the burden of proof, procedures of prosecution and rights of the accused are considerably different in civil and criminal contempt cases, *Parker,*

supra, 153 F.2d at 70-71, *McIntosh,* like *O'Hagen, supra,* has no relevance here.

The Third Circuit has, in another contempt case, adopted the same procedure used here. In *In re Contemporary Apparel, Inc.,* 488 F.2d 794, 799 (3d Cir. 1973), the court remanded a civil contempt case, also under Section 41 of the Act, 11 U.S.C. §69, to the district court so that it might "reconsider the referee's certificate of facts showing contempt, and then provide whatever remedy it believes, in its sound judgment, is warranted."

Rules 11-44 and 920 are thus constitutional and were constitutionally applied here. The court of appeals properly held that Petitioners' knowing and wilful violation of Rule 11-44 constituted civil contempt for which appropriate remedial sanctions were applied.

5. Petitioner Hubbard Cannot Be Excused from the Consequences of His Acts.

Petitioner Hubbard seeks to avoid being penalized for his contemptuous conduct by relying on his status as counsel to Camelia and Farnale. He cites *In re Watts & Sachs,* 190 U.S. 1 (1903). But the *Watts* case, a criminal contempt case, is distinguishable from this civil contempt case because the alleged contemnors there were sentenced to imprisonment. Here, FMI only sought an order directing Petitioner Hubbard to discontinue the Mississippi Action, to restore to FMI those monies it was deprived of in the Mississippi Action, and to reimburse FMI for those costs which it had to incur as a result of his conduct. Because of the greater burden of proof in a criminal contempt case,

the Court in *Watts* found insufficient evidence to sustain the conviction. 190 U.S. at 35. The Court did not hold, however, that an attorney may be insulated from the court's contempt power.

Petitioner Hubbard also cites *Imbler* v. *Pachtman,* 424 U.S. 409 (1976), which was a civil rights action, decided under 42 U.S.C. §1983, and not a contempt case. The Court in *Imbler* held that a *public prosecutor* was immune from a suit for damages under 42 U.S.C. §1983, but did not even imply that the prosecutor would be immune from a contempt citation if he refused to obey a court order or rule. Hence, Petitioner Hubbard cannot rely on *Imbler* to insulate himself from liability.

Petitioner Hubbard's conduct undoubtedly interfered with and obstructed the bankruptcy court's administration of the debtor's estate. Specifically, Hubbard counselled his clients to violate the specific stay of Rule 11-44 rather than to seek a modification thereof under the prescribed procedure. The district court found Petitioner Hubbard "equally in contempt with the clients he counselled," (Appendix III at 38a) and cited with approval the language of the bankruptcy court opinion:

> "I think he played fast and loose with the Rules. . . .
>
> "This court is loathe to certify an attorney for contempt but if an attorney will not recognize and honor the obligation to obey the automatic stay provisions of the Rules, how could a layman be expected to do so."

B. Petitioners' Reliance on 28 U.S.C. §959 Is Misplaced.

1. FMI, as Debtor-in-Possession, Was Not Conducting Business Within the Meaning of 28 U.S.C. §959.

The court of appeals correctly concluded here that, based on the facts of this case, 28 U.S.C. §959 did not authorize Petitioners to commence the Mississippi Action. Although that provision permits suits against debtors-in-possession for their acts in carrying on their business, it was not applicable here because Petitioners were merely attempting to enhance their position as against other creditors of FMI.

28 U.S.C. §959 provides in pertinent part as follows:

> a. Trustees, receivers or managers of any property, including debtors-in-possession, may be sued, without leave of the court appointing them, *with respect to any of their acts or transactions in carrying on business connected with such property.* Such actions shall be subject to the general equity power of such court so far as the same may be necessary to the ends of justice, but this shall not deprive a litigant of his right to trial by jury. [Emphasis supplied.]

Section 959 was intended to create an exception to the general rule that law suits against receivers or trustees in bankruptcy could not be brought without leave of the court. *Vass* v. *Conron Bros. Co.*, 59 F.2d 969, 970 (2d Cir. 1932). The intended exception was a narrow one, however, limited only to those actions against receivers, trustees or debtors-in-possession which are directly related to acts or transactions of such fiduciaries in their carrying on of the business connected with the property entrusted to them. *In re*

Investors Funding Corp. of New York, et al., —— F.2d —— (2d Cir. Dec. 15, 1976) (No. 76-5019, Slip. Op. 983); *Austrian* v. *Williams*, 216 F.2d 278 (2d Cir. 1954), *cert. denied*, 348 U.S. 953 (1955); *Vass* v. *Conron Bros. Co.*, 59 F.2d 969 (2d Cir. 1932); *In re American Associated Systems, Inc.*, 373 F.Supp. 977 (E.D. Ky. 1974); *see also* 2 Collier, Bankruptcy ¶2.36 at 247-48 (14th rev. ed. 1975).

The allegations of Petitioners' complaint in the Mississippi Action did not relate to or arise from an act of the debtor-in-possession in carrying on the business of the debtor. Rather, Camelia and Farnale were attempting to subordinate FMI's deed of trust and to enforce a purported mechanics' lien on the subject property arising from work performed *before* the commencement of the Chapter XI case. Appendix IV at 44a.

The foregoing is confirmed by the relief sought in the Mississippi state court action begun by Camelia and Farnale against the debtor prior to the commencement of the FMI Chapter XI case. Before filing its Chapter XI petition, FMI had commenced preparations for nonjudicial foreclosure against the real property in Mississippi subject to its lien. In the two suits started by Camelia and Farnale in the state and federal courts, they sought (1) an order enforcing their purported mechanics' and materialmen's lien against the subject property; and (2) a monetary judgment against the debtor. Appendix IV at 43a. The striking similarity in relief sought by Petitioners in the two actions—one of which was started *prior* to FMI's filing its Chapter XI petition—undermines their contention that the Mississippi Action relates to an act or transaction of FMI,

as debtor-in-possession, which is a requirement of 28 U.S.C. §959. Thus, Petitioners sought the same relief against FMI, debtor-in-possession, as they did against FMI, debtor.

Assuming, *arguendo,* that the Mississippi Action relates to FMI's conduct as debtor-in-possession, the cases construing 28 U.S.C. §959 nevertheless demonstrate that FMI's conduct does not come within the purview of the subject statute. As stated by the court of appeals here:

> The evident purpose of §959 is to enable a debtor-in-possession to continue his business subsequent to the filing of a Chapter XI petition. If debtors-in-possession were immunized from all suits after filing Chapter XI petitions, it would be difficult, if not impossible, for them to remain in business. Suppliers would be less likely to provide merchandise, banks would be less likely to extend credit and workers would be less likely to undertake employment with a debtor-in-possession if they were foreclosed from suing the debtor for wages or other obligations incurred after the Chapter XI petition is filed.
>
> Hence, §959 makes debtors-in-possession suable for the routine occurrences which arrise [sic] from efforts to continue "carrying on business" after the Chapter XI petition is filed.
>
> However, §959 was not intended to serve as *carte blanche* for creditors seeking to sue debtors-in-possession in a forum of creditors' choosing.

Appendix I at 18a.

Thus, the authority conferred by 28 U.S.C. §959 upon third parties permits them to hold a debtor-in-possession accountable for torts which it commits in the furtherance of its business operations. It was not meant to foster in-

terference with the use, control, maintenance and operation of the debtor's property. *See In re American Associated Systems, Inc.,* 373 F.Supp. 977, 979 (E.D. Ky. 1974); *see also* 2 Collier, Bankruptcy ¶2.36 at 248 (14th rev. ed. 1975). Petitioners' belated allegation that FMI committed a tort (Petition at 31) is merely an afterthought. This allegation was first raised in the court of appeals and was never mentioned in either the Mississippi Action or in the other courts below. Furthermore, when a trustee or debtor-in-possession* does that which is necessary to maintain the assets of an estate for the benefit of its creditors, those acts cannot be grounds for the commencement of a plenary action under the 28 U.S.C. §959 exception. *In re Investors Funding Corp. of New York, et al.,* —— F.2d —— (2d Cir. Dec. 15, 1976) (No. 76-5019, Slip Op. 983); *Austrian* v. *Williams,* 216 F.2d 278 (2d Cir. 1954), *cert. denied,* 348 U.S. 953 (1955); *Vass* v. *Conron Bros. Co.,* 59 F.2d 969 (2d Cir. 1932); *In re American Associated Systems, Inc.,* 373 F. Supp. 977 (E.D. Ky. 1974); *Melvin* v. *Klein,* 266 N.Y.S. 2d 533 (Sup. Ct. 1965).

The Second Circuit recently discussed the scope of §959 in the *Investors Funding Corp.* case, *supra.* There, the court assumed that a pending plenary action outside of the reorganization court related "to a routine ongoing business activity of the reorganized estate," noting that if "the suit were not so related," it could affirm the district court's injunction "without further inquiry." *In re Investors Fund-*

* A debtor-in-possession has not only the "title and powers" of a trustee, but also the "rights, duties and remedies" of a trustee in bankruptcy. *In re J. R. Cianchette & Sons Corp.,* 198 F.Supp. 740, 742 (D. Me. 1961); *In re Martin Custom Tires Corp.,* 108 F.2d 172, 173 (2d Cir. 1939).

ing Corp., supra at 988. Despite its assumption, the court still affirmed the injunction against the plenary action, reasoning as follows:

> But the main purpose of the suit brought against the trustee here is to revamp or alter a substantial interest in property administered by the court, which must necessarily lead to embarrassment to the estate. *See Ex parte Baldwin,* 291 U.S. 610, 618 (1934) (Brandeis, J.). The suit is designed to revise the trustee's interest in an item of intangible property, a wrap-around mortgage, by "unwrapping" it, thereby changing not only the value of the res by a very substantial amount ($700,000), but also changing the trustee's performance of his servicing duties in the future. Damages for the act of the trustee in omitting to make the timely payment to Buffalo would be only incidental to the real relief sought in the state court suit, just as the damages sought for failure to maintain contractually mandated passenger service in *Ex parte Baldwin, supra,* were incidental to the forfeiture of the railroad right-of-way that was sought as a remedy for the breach of contract, *id.*

Id., Slip Op. at 988-89. The foregoing reasoning is directly applicable here. Petitioners sought in the Mississippi Action to subordinate FMI's security interest, despite the fact that such property was subject to the Chapter XI court's jurisdiction.

In *Vass* v. *Conron Bros. Co.*, 59 F.2d 969 (2d Cir. 1932), the bankrupt had operated a cold meat storage plant and had leased to Conron Bros. Co. a portion of the premises which the bankrupt had agreed to refrigerate. After the trustee in bankruptcy affirmed the bankrupt's lease, Conron alleged that the trustee had failed to refrigerate the premises properly, causing the goods to spoil. Conron then commenced an action in the state court in reliance upon 28 U.S.C. §125, the predecessor to Section 959, having mistakenly presumed that the trustee's assumption of the bankrupt's lease made him amenable to suit. The court rejected Conron's contention, however, and affirmed the bankruptcy court's order staying the prosecution of the state court action.

Holding that Conron's claim did not arise from an "act or transaction" of the trustee in carrying on the business of the bankrupt, the court set forth guidelines for determining what action may be taken by a trustee without exposing himself to suits under 28 U.S.C. §959:

> To "carry on the business" is, we should think, the same thing as to "continue" it under Section 2(5) of the Bankruptcy Act, 11 USCA §11(5); it must involve enough to require an order of court. [Citations omitted.] *Merely to hold matters in statu quo; to mark time as it were; to do only what is necessary to hold the assets intact; such activities do not seem to us to be a continuance of the business.* This was all that [the trustee] did. When he took over the refrigerating plant, he found a lessee in possession of a part of them, from which he could not eject it. His alternatives were to accept the reversion, cum onere, as he did, making himself liable on covenants; or to reject it, leaving the bankrupts reversioners pro tanto, and owners of a most inconvenient interest in a building otherwise his own. He did no more than avoid this absurd complication, which would surely have impeded the settlement of the estate, and the discharge of his duties. It seems plain that he was not carrying on business as [28 U.S.C. §959] uses that term. . . . [Emphasis supplied.]

59 F.2d at 971. Thus, a debtor-in-possession which merely holds "the assets intact" cannot be deemed to be continuing its business.

Here, FMI was also merely preserving the assets of the estate. FMI's borrower defaulted on a loan in excess of $1,000,000, which was secured by a first deed of trust. In order to preserve its asset, FMI had no alternative but to proceed against the collateral by commencing the trustee's sale. For FMI to have done otherwise would have been a breach of its fiduciary obligation as a debtor-in-possession to protect and preserve its assets for the benefit of its creditors, an obligation imposed upon a debtor-in-possession whether or not authorized to operate the business of the debtor. *See generally Gardner-Denver Co.* v. *C. J. Haslam, Inc.*, 325 F.2d 208 (2d Cir. 1963); *In re Roosevelt Lanes, Inc.*, 234 F.Supp. 842 (E.D.N.Y. 1964), *aff'd per curiam*, 342 F.2d 1000 (2d Cir. 1965); 8 Collier, Bankruptcy ¶6.32 at 928-29 (14th rev. ed. 1975).

Likewise, in *Austrian* v. *Williams*, 216 F.2d 278 (2d Cir. 1954), *cert. denied*, 348 U.S. 953 (1955), the Second Circuit reaffirmed its holding in *Vass, supra*, that the collection and liquidation of assets is not "carrying on business" within the meaning of 28 U.S.C. §959. In *Austrian*, the Chapter X reorganization trustees had commenced a plenary action in federal court against the debtor's former officers, directors and principal stockholders, charging them with various derelictions in their management of the debtor's affairs. A trial on the trustee's claim resulted in a dismissal, and the defendants thereafter asserted claims in the federal action against the trustees, alleging, *inter alia*, that by commencing the plenary action the trustees forfeited their

immunity from liability in any court where the controversy was heard. The court rejected the defendants' contentions, holding that the suit commenced by the trustees did not constitute "'carrying on the business of the debtor.'" 216 F.2d at 285. The court, through then Circuit Judge Harlan, cited *Vass* v. *Conron Bros. Co., supra*, stating: "Merely to attempt to collect and liquidate the assets of a debtor is not to carry on its business in any proper sense of the term." 216 F.2d at 285. Thus, FMI's foreclosure sale falls squarely within the holding of *Austrian*: both actions sought "to collect and liquidate the assets of [the] debtor" and did not constitute carrying on the debtor's business.*

In a case similar to the instant case, the trustee in *In re American Associated Systems, Inc.*, 373 F.Supp. 977 (E.D. Ky. 1974), sought to have certain persons adjudged in contempt because of their violation of a stay order entered in the pending bankruptcy case. The contemnors had commenced actions in the state court against the trustee in bankruptcy and the bankruptcy judge, among others, subsequent to the dismissal of previous actions which had been commenced by the trustee for the collection of certain amounts due on promissory notes allegedly held by the contemnors and owed to the bankrupt. Because the trustee was unsuccessful in the litigation on the promissory notes, the contemnors alleged in their actions that the trustee and bankruptcy judge were guilty of libel, slander, malicious prosecution and conspiracy. In the contempt proceeding,

* As set forth in Exhibit "A" annexed to FMI's Chapter XI petition, the debtor was "engaged in mortgage lending for construction and development of real estate, and in ownership and the attendant operations of ownership of real property." Appendix IV at 42a. Petitioners' suggestion that FMI's foreclosure constituted the carrying on of its business is as illogical as stating that a lessor of real property is in the business of dispossessing its tenants.

the contemnors alleged that their malicious prosecution actions did not involve the "title, possession, or control of the *res* but a tort committed by the trustee in operating the debtor's business." 373 F.Supp. at 978.

The court rejected the contentions of the contemnors and adjudged them in contempt, reasoning that a trustee has an "official responsibiilty" to collect and reduce to money the property of the estate, and that this duty has nothing to do with the conduct of the bankrupt's business.

> To this end, the trustee must institute necessary legal actions including those arising from contract. . . . "Rights of action arising upon the contracts or property of the bankrupt, not yet resolved into suit, pass to the trustee and he should assert them in the proper tribunal whenever necessary for the collection or preservation of the bankrupt estate." [Citations omitted.] Thus, the commencement of suit in state court for recovery of sums allegedly due the bankrupt was commanded by the statutory directive to liquidate the estate assets, and is not classifiable as "carrying on business" as contemplated by 28 U.S.C. 959(a).

373 F.Supp. at 978-79. Here, the right of FMI, as debtor-in-possession, to foreclose arose from the deed of trust between the debtor and its borrower. Thus, the courts below correctly determined that the commencement of the foreclosure by FMI was merely an enforcement of that right and, in foreclosing, FMI was merely fulfilling its duty to protect and preserve its assets for its creditors.

2. *Petitioners' Enforcement of a Lien on Property Does Not Come Within the Scope of Section 959.*

A debtor's mortgage or lien is a property interest subject to the jurisdiction of the bankruptcy court. *In re Westec Corp.*, 460 F.2d 1139 (5th Cir. 1972); *In re Prudence-Bonds Corp.*, 77 F.2d 328, 330 (2d Cir. 1935); *and see Segal* v. *Rochelle*, 382 U.S. 375, 379 (1966) (discussed in I.A.2., *supra*). Petitioners sought in the Mississippi Action to subordinate FMI's lien to their purported lien, and thus sought to enforce a lien on the property of FMI, as debtor-in-possession, property that was *in custodia legis*. Actions against property within the bankruptcy court's jurisdiction, however, are *not* permissible under 28 U.S.C. §959.* *See Field* v. *Kansas City Refining Co.*, 9 F.2d 213 (8th Cir.), *cert. denied*, 271 U.S. 676 (1925); *Field* v. *Kansas City Refining Co.*, 296 F. 800 (8th Cir.), *cert. denied*, 266 U.S. 618 (1924); *J. I. Case Plow Works* v. *Finks*, 81 F. 529 (5th Cir. 1897); *In re American Associated Systems, Inc.*, 373 F. Supp. 977 (E.D. Ky. 1974); *American Brake Shoe & Foundry Co.* v. *Interborough Rapid Transit Co.*, 10 F.Supp. 512 (S.D.N.Y.), *aff'd per curiam*, 76 F.2d 1002 (2d Cir.), *cert. denied*, 295 U.S. 760 (1935); *Dickinson* v. *Willis*, 239 F. 171 (S.D. Iowa 1916); *Love* v. *Louisville & E.R. Co.*, 178 F. 507 (W.D. Ky. 1910).

In *American Brake Shoe & Foundry Co.* v. *Interborough Rapid Transit Co.*, 10 F.Supp. 512 (S.D.N.Y.), *aff'd per curiam*, 76 F.2d 1002 (2d Cir.), *cert. denied*, 295 U.S. 760

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* In fact, Rule 11-61(a)(2) of the Rules of Bankruptcy Procedure expressly provides that a proceeding to "determine the validity, priority, or extent of a lien or other interest in property" is an "adversary proceeding" governed by "Part VII of the Bankruptcy Rules."

(1935), the court held that the predecessor to 28 U.S.C. §959 did not contemplate the allowance of suits, such as the Mississippi Action, intended to establish liens or possessory rights in the *res* subject to the bankruptcy court's jurisdiction.

> As uniformly interpreted by the courts, . . . [the] sole purpose [of 28 U.S.C. §959] is to make federal receivers amenable to state court suits on causes of action arising out of the ordinary operation of the company in receivership. Actions for personal injuries caused by the negligent operation of a common carrier are a familiar example. Gableman v. Peoria, Decatur and Evansville R.R. Co., 179 U.S. 335, 21 S.Ct. 171, 45 L. Ed 220 (1900). On the other hand, causes directly affecting the administration of the receivership res, or property rights therein, do not fall within the provision; *to allow such suits to be instituted without leave of the court which has the property in its custody would divest it of its exclusive jurisdiction thereover and lead but to conflict and confusion in administration.* Such was not the legislative purpose. [Emphasis supplied.]

10 F.Supp. at 518.

None of the authorities cited by Petitioners supports their reliance on Section 959. The Mississippi and Texas state court cases cited by Petitioners have no relevance to the issues in this case. *In re Liebig,* 255 F. 459 (2d Cir. 1918) (Petition at 29), and *In re Commonwealth Bond Corp.,* 77 F.2d 308 (2d Cir. 1935) (Petition at 31), were, in any event, necessarily superseded by the Second Circuit's decision in this case and in *Austrian* v. *Williams, supra.*

Liebig, supra, was a reclamation action commenced *in the bankruptcy court* in order to recover a fraudulent purchase of eggs by the bankrupt. A direct contractual relationship existed between the parties there, but no contractual relationship existed between FMI and Camelia and Farnale. In sum, *Liebig* bears no relationship to any issue before this Court.

In re Commonwealth Bond Corp., supra, involved property held in trust by the debtor for another person. It was not, therefore, property of the debtor and, accordingly, not subject to the bankruptcy court's exclusive jurisdiction. The excerpt from *Commonwealth Bond Corp.* that Petitioners have taken out of context (Petition at 31) takes on a different meaning when read in context with the sentences preceding and following it:

> But the [injunctive] power so exercised was necessarily founded upon the possibility of bringing the security, suits against which were enjoined, within a plan of reorganization. . . . Since property held by the debtor as fiduciary cannot be included [within a plan of reorganization], suits confined to its administration may not be stayed.

77 F.2d at 309-10. In contrast, FMI had absolute ownership of the deed of trust here and did not hold it as a fiduciary. Petitioners commenced the Mississippi Action not against any property held in trust by FMI for some third party, but against FMI and its property. FMI's deed of trust, and the real property securing it, can and will be brought within FMI's Chapter XI plan.

The remaining authorities relied on by Petitioners are equally inapposite. *Diners Club, Inc.* v. *Bumb,* 421 F.2d 396 (9th Cir. 1970), and *Novo Enzyme Corp.* v. *Baker,* 361 F. Supp. 337 (S.D.N.Y. 1973), shed no light on the issues in

this case. The reorganization trustees in those cases were sued in state courts for breach of contracts which they had made. No such facts are present here. FMI, as debtor-in-possession, never entered into or assumed any contracts with Petitioners.

The foregoing authorities confirm that the commencement of the Mississippi Action by Petitioners violated the stay provisions of Rule 11-44, and that such conduct did not fall within the specific exceptions set forth in 28 U.S.C. §959.

3. *Asserted Good Faith Does Not Excuse Disobedience of the Automatic Stay of Rule 11-44.*

Petitioners' mistaken reliance on 28 U.S.C. §959 in commencing the Mississippi Action does not excuse or mitigate their deliberate disobediance of Rule 11-44.

In *In re American Associated Systems, Inc., supra,* the contemnors conceded that they had commenced their state court action with full knowledge of the bankruptcy court's stay order but, like Petitioners here, erroneously relied on 28 U.S.C. §959, arguing that the stay did not prohibit them from commencing the action. In finding contempt, the court held that 28 U.S.C. §959 was inapplicable, and that, accordingly, the "commencement of [the] state court actions against the trustee was a direct violation of the . . . [stay] order." 373 F.Supp at 979.

The court in *American Associated Systems* recognized that the contemnors' conduct may have been in good faith but that their actions still constituted contempt of court, reasoning as follows:

> It is equally apparent that the deliberate disobedience by respondents . . . is not mitigated by their subjective legal conclusions. Unlike its criminal counterpart, *civil contempt is " 'wholly remedial,' serves only the purpose of a party litigant, and is intended to coerce compliance with an order of the court or to compensate for losses or damages caused by non-compliance."* [Citations omitted.] [T]he good faith underlying the respondents' determination to sue in the Kentucky court does not diminish their culpability. [Emphasis supplied.]

373 F.Supp. at 979. Thus, the intentions of the Petitioners in doing the prohibited act are of no consequence if the act is in contravention of the court's order. *See McComb* v. *Jacksonville Paper Co.,* 336 U.S. 187, 191 (1949); *NLRB* v. *Local 282,* 428 F.2d 994, 1000-01 (2d Cir. 1970) ("a violation need not be wilful for a party to be found in civil contempt."); *NLRB* v. *Ralph Printing & Lithographing C.,* 433 F.2d 1058, 1062 (8th Cir. 1970), *cert. denied,* 401 U.S. 925 (1971); *United States* v. *Ross,* 243 F.Supp. 496, 499 (S.D.N.Y. 1965) ("In civil contempt proceedings the question is not one of intent but whether the alleged contemnors have complied with the court's order.").

Furthermore, Petitioners' purported reliance on Mississippi law in an attempt to demonstrate the substantive validity of their asserted mechanics' and materialmen's lien is irrelevant to the contempt citation here. As the Second Circuit correctly held:

> The issue here is a procedural one: whether Camelia and Farnale should have secured permission from the New York bankruptcy court before proceeding with their action in Mississippi. . . . That Camelia and

> Farnale may have a valid substantive position under Mississippi law does not mitigate, excuse or justify their willful procedural violation of the federal bankruptcy rules.

Appendix I at 20a-21a. *See Oriel* v. *Russell,* 278 U.S. 358, 363 (1929); 1 Collier, Bankruptcy ¶2.58 at 315 (14th rev. ed. 1974).

Thus, the Second Circuit properly affirmed the judgment of the district court which held that Petitioners' wilful and deliberate violation of the stay provisions of Rule 11-44 "only indicates . . . a contemptuous attitude to Rules which have the sanction of the Supreme Court and of the Congress of the United States." Appendix III at 38a.

II.

No Reason Exists for the Issuance of a Writ of Certiorari.

The considerations governing review on certiorari, set forth in this Court's Rule 19.1(b), though not limiting the discretion of the Court, do support a denial of certiorari here. No conflict exists between the Second Circuit's decision and decisions of this Court or of other courts of appeals. As shown in I., *supra,* the decision of the court of appeals was based on well-established principles of law.

Petitioners have also failed to cite any applicable cases in support of their purported constitutional and jurisdictional arguments. The Second Circuit's decision deals with no important question of federal law which has not been, but should be, settled by this Court, and Petitioners make no such contention.

Three courts have examined the facts herein,* and each has determined that those facts conclusively demonstrate that Petitioners had knowledge of "FMI's Chapter XI petition in New York almost immediately after it was filed" and of the automatic stay provisions of Rule 11-44, yet they wilfully violated the procedures established by the Rules of Bankruptcy Procedure. Appendix I at 20a. As Mr. Justice Holmes wrote in *United States* v. *Johnston,* 268 U.S. 220, 227 (1925):

> We do not grant a certiorari to review evidence and discuss specific facts.

That the Second Circuit and the district court here did not depart from the accepted and usual course of judicial proceedings is demonstrated by the denial of Petitioners' motions for rehearing and rehearing *en banc* by the court of appeals. Appendix II at 30a-31a.

Finally, there is no conflict among the circuits or with this Court on the issues presented. For clarity, the purported conflicts, as set forth in Point 3 of the Petition, pages 13-15, between the Second Circuit's decision and decisions of this Court and of other circuits are analyzed seriatim:

1. *Straton* v. *New,* 283 U.S. 318 (1931), does not hold that a state court action instituted prior to the commencement of a Chapter XI case preempts subsequent assumption of jurisdiction by a bankruptcy court. *Straton,* decided before the passage of the Chandler Act in 1938, dealt with

* Petitioners' allegation (Petition, Point 8, at 32-33) that James Young, an attorney who represented FMI in the Mississippi Action, has a conflict of interest is patently false and not worthy of reply.

the bankruptcy court's jurisdiction in an ordinary bankruptcy case under Chapters I-VII of the Act. That jurisdiction is limited to property in the bankrupt's "actual or constructive possession." *Thompson* v. *Magnolia Petroleum Co.*, 309 U.S. 478, 481 (1940). Under Section 311 of the Act, however, the Chapter XI court has "exclusive jurisdiction" of the debtor's property "wherever located." *See In re Freed & Co.*, 534 F.2d 1235, 1239 (6th Cir. 1976). Additionally, the Court in *Straton* was careful to state that "the action in the state court was merely in the nature of an execution or proceeding to obtain the avails of the judgment lien. . . ." 283 U.S. at 327. The creditors in *Straton* had gotten judicial liens sixteen months prior to bankruptcy. Petitioners' action in the Mississippi state court, however, was commenced within a month before the filing of FMI's Chapter XI case, had not proceeded to judgment, and no receiver had been appointed therein.

2. Neither this Court's decision in *Maggio* v. *Zeitz*, 333 U.S. 56 (1948), nor the Third Circuit's decision in *In re Rubin*, 378 F.2d 107 (3d Cir. 1967), held that all property issues must be disposed of prior to institution of contempt proceedings. In *Maggio*, this Court held that the bankruptcy court must determine whether a party is able to comply with a turnover order before adjudging that party in contempt for failing to comply. No such issue exists here. The only property issue, whether FMI's deed of trust constituted property of the debtor, was decided in the affirmative by the courts below.

The property question in *Rubin* was whether particular delivery routes were property of the debtor and, accordingly, whether persons were restrained from interfering with those delivery routes. The courts here did deal with the issue of whether FMI's deed of trust constituted property of the debtor protected by the automatic stay of lien enforcement in Rule 11-44. Thus, the decision below is not in conflict with either *Maggio* or *Rubin*.

3. Neither *Magen* v. *Campbell*, 186 F. 675 (3d Cir. 1911), nor *Wakefield* v. *Housel*, 288 F. 712 (8th Cir. 1923), held that contempt proceedings are prohibited under Section 41a of the Act for violation of the injunctive provisions of the Rules of Bankruptcy Procedure. In *Magen*, the alleged contemnor had been charged with refusing to be examined according to law. The Third Circuit held that the facts showed that the charge should have been perjury. Because the contempt proceedings had been summary, and a perjury charge would entitle the alleged contemnors to all the rights of a criminal defendant, the court reversed, but stated that had the charge of refusal to be examined been correct, the judgment under review might have stood.

Similarly, the Eighth Circuit in *Wakefield*, a *criminal* contempt case, reversed the judgment of the district court because the proceedings afforded the alleged contemnor had been *civil* in nature, thus depriving the alleged contemnor of his rights. Certainly neither case conflicts with the Second Circuit's decision here.

4. *In re A. Roth Co.*, 125 F.2d 396 (7th Cir. 1942); *Town of Agawam* v. *Connors*, 159 F.2d 360 (1st Cir.), *cert. denied*, 330 U.S. 845 (1947); *Brunn* v. *Wichser*, 75 F.2d 25 (3d Cir. 1934); and *In re Stanndco Developers, Inc.*, 534 F.2d 1050 (2d Cir. 1976), all cited by Petitioners, do not hold that Rule 11-44 is inapplicable in the case of competing lien

claimants. Indeed, the competing lienholder in *Roth* knowing that she was stayed from any foreclosure action that would affect the bankrupt's property, applied to the bankruptcy court for authority to commence her foreclosure action. The Seventh Circuit in *Roth* merely held that the bankruptcy court should have granted the competing lienholder leave to foreclose. Contrary to Petitioners' interpretation of *Roth*, the court there acknowledged the bankruptcy court's jurisdiction over the bankrupt's property, a junior mortgage, and the need for a competing lienholder to apply to the bankruptcy court if it wished to foreclose on real property in which the bankrupt had a mortgage interest.

Agawam and *Brunn* were not Chapter XI or Chapter X cases. In neither case did the court have jurisdiction of the debtor's property "wherever located," as did the Chapter XI court here. Thus, neither case conflicts with the Second Circuit's decision.

Stanndco, supra, like *Roth, Agawam,* and *Brunn,* is not a contempt case. The Second Circuit in *Stanndco,* a Chapter X case, did not hold that the bankruptcy court had no jurisdiction to stay suits against the debtor and its property, but merely modified the stay of suits to permit a foreclosure action to proceed against the debtor's "surety without any concurrent personal judgment taken against the debtor or trustee." 534 F.2d at 1054. Thus, *Stanndco* is easily reconciled with the instant case. Petitioners' statement that the bankruptcy court has no jurisdiction to restrain state court proceedings seeking to enforce liens on property *not* belonging to the debtor has no relevance here

because the Second Circuit held that Petitioners had sought to enforce a lien on property which *did* belong to FMI. Indeed, the court in *Stanndco* recognized that a reorganization court may stay a suit which has "as its immediate objective a judgment against the debtor, or interference with property of the debtor which is under the reorganization court's jurisdiction." 534 F.2d at 1052.

5. Contrary to Petitioners' suggestion, the Second Circuit's holding that Camelia and Farnale were required to secure a modification of the Rule 11-44 automatic stay of lien enforcement before commencing or continuing their action against FMI is not in conflict with *Perry* v. *Wood,* 63 F.2d 257 (5th Cir. 1933); *In re Grissler,* 136 F. 754 (2d Cir. 1905); *Hicks* v. *Knost,* 178 U.S. 541 (1900); *Taylor* v. *Carryl,* 61 U.S. 589 (1858); or *In re Willax,* 93 F.2d 293 (2d Cir. 1937).

Willax and *Grissler, supra,* are earlier Second Circuit decisions and, therefore, present no conflict between circuits. Neither is *Perry* v. *Wood, supra,* in conflict with the Second Circuit's holding here. In *Perry,* the bankrupt and a lienholder each had claims against a sum of money which was deposited with the clerk of a state court prior to the filing of an *involuntary petition in bankruptcy* under Chapters I-VII of the Act against the bankrupt. Because the jurisdiction of the bankruptcy court was limited to property within the bankrupt's possession, it could not stay the prebankruptcy court proceedings. In contrast, FMI's property here was only required to be deposited with the Mississippi federal court pursuant to court order *after* the commencement of FMI's Chapter XI case.

Hicks v. *Knost, supra,* held that a trustee cannot bring an action in the bankruptcy court for *in personam* relief against a third party asserting an adverse claim of ownership to the subject property without the adverse claimant's consent. Thus, the issue in *Hicks* v. *Knost* was not before the court of appeals here. Neither *Hicks* v. *Knost* nor *Taylor* v. *Carryl, supra,* which is not a bankruptcy case, dealt with a Chapter XI court's jurisdiction to *stay* actions against the debtor and its property. Hence, their holdings do not conflict with that of the Second Circuit here. In fact, if Petitioners had read *White* v. *Schloerb,* 178 U.S. 542 (1900), which was decided by this Court immediately after *Hicks, supra,* they would have seen that the Court was "of opinion that the judge of the court of bankruptcy was authorized to compel persons who had forcibly and unlawfully seized and taken out of the judicial custody of that court property which had lawfully come into its possession as part of the bankrupt's property, to restore that property to its custody; and therefore . . . 'the district court sitting in bankruptcy had jurisdiction by summary proceedings to compel the return of the property seized.' " 178 U.S. at 548. The district court here has done precisely what the district court was authorized to do in *White* v. *Schloerb*: it required Petitioners to return to FMI its funds wrongfully taken after the filing of the Chapter XI petition.

6. As in *Perry* v. *Wood, supra,* the court in *Mid-Jersey National Bank* v. *Fidelity Mortgage Investors,* 518 F.2d 640 (3d Cir. 1975), held that funds deposited with a court prior to the filing of the Chapter XI petition were not property of the debtor. Therefore, the court held that Rule 11-44 was not applicable. The Second Circuit considered

the holding of *Mid-Jersey* (Appendix I at 13a-14a) and noted that "here, unlike the situation in [*Mid-Jersey*], there is a property interest of FMI's existing at the date of institution of the Chapter XI proceeding which gives the bankruptcy court jurisdiction and which therefore makes Rule 11-44 applicable." Accordingly, there is no conflict between the Second and Third Circuits.

7. *In re McIntosh,* 73 F.2d 908 (9th Cir. 1934), was a criminal contempt case decided long before the effective date of Rule 920. Because *McIntosh* involved criminal contempt, the court limited its findings to such cases. 73 F.2d at 910. Thus, the Second Circuit's holding here is not in conflict with the Ninth Circuit's holding in *McIntosh.*

8. Finally, neither *In re Watts & Sachs,* 190 U.S. 1 (1903), nor *Imbler* v. *Pachtman,* 424 U.S. 409 (1976), is in conflict with the Second Circuit's holding. *Watts* was a criminal contempt case in which the contemnors were sentenced to imprisoment; there existed no restraining order, injunction or rule which had been violated by the alleged contemnors. Additionally, there was a conflict of evidence in *Watts* that does not exist here. The Court merely found that "there was no legal evidence to sustain this conviction for contempt. . . ." 190 U.S. at 35.

Imbler, supra, was not a contempt case, but rather a civil rights action. The Court concluded there that a public prosecutor was immune from a suit for damages under 42 U.S.C. §1983. It did not hold that a public prosecutor or an attorney was insulated from civil contempt liability for a wilful violation of an order or rule of the court.

The foregoing discussion confirms that the court of appeals decision here is not in conflict with any decisions of this Court or of any other court of appeals. Moreover, there was no departure in this case from existing law, and there is no important question of federal law which has not been, but should be, settled by this Court. Accordingly, this Court should not grant certiorari.

Conclusion

For the reasons stated, the petition for a writ of certiorari to the Court of Appeals for the Second Circuit should be denied.

Dated: New York, New York
January 13, 1977

Respectfully submitted,

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APPENDIX

Decision of the United States Court of Appeals for the Second Circuit on Petition for Rehearing

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 1028 — September Term, 1975

(Argued May 13, 1976 Decided September 3, 1976)

Decision-Petition for Rehearing
November 5, 1976

Docket No. 76-5007

IN RE:

FIDELITY MORTGAGE INVESTORS,

Debtor,

FIDELITY MORTGAGE INVESTORS,

Applicant-Appellee,

v.

CAMELIA BUILDERS, INC., E. J. YELVERTON, JR., FARNALE, INC., R. L. GOODALE and JEFFREY H. HUBBARD,

Respondents-Appellants.

Before: SMITH, MANSFIELD and VAN GRAAFEILAND,

Circuit Judges.

ON REHEARING

PER CURIAM:

The petition for rehearing is denied. The opinion is corrected by striking the period on page 5390 of the slip opinion, line 27, inserting a semicolon, and striking the

language from "Rule 602(a) . . ." on line 27 to and including "Moreover," on line 31, so that the paragraph will read:

> "There is no merit to this position; as the *Rubin* decision makes clear, a person is in contempt of court if he knowingly violates a court order, whether or not he received a formal notice. The cases do not require that the contemnors have received formal notice if they have actual knowledge of the order. Hence, the issue of formal notice is irrelevant to Camelia and Farnale's contempt since it is clear that they, in fact, did know of the stay which they ignored."

/s/ J. Joseph Smith

J. Joseph Smith

/s/ Walter R. Mansfield

Walter R. Mansfield

/s/ Ellsworth A. Van Graafeiland

Ellsworth A. Van Graafeiland

Circuit Judges.